MANUFACTURERS HANOVER

# Financial Digest

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Analysis of Business Trends Plus Selected Financial Indicators

## The Road To More Inflation Is Paved . . .

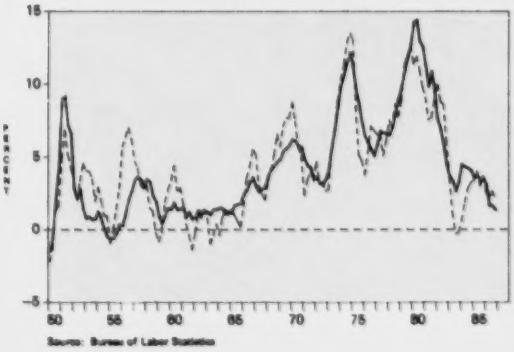
Most economic indicators are abstract figures in the minds of many Americans. Few, if any, feel personally affected by moderate GNP growth or a rise in durable goods orders. But anyone who buys anything can understand inflation. The evidence is as close as the local supermarket or corner drug store. So it is understandable that recent talk of a return to rising inflation has not only affected the bond market and precious metals—it has also raised fears for everyone carrying a wallet.

Many factors have been advanced in the arguments for expecting that price rises in 1987 will run well above the 1.9 percent average of 1986. First, because falling energy prices almost single-handedly held down inflation last year, the recent rise of oil prices—spot prices for West Texas oil are now 56 percent above their year-ago levels—portends a return to more inflation. Second, the lower exchange rate of the U.S. dollar has begun to translate into higher prices for imported goods. Next is the monetarist argument that the rapid run-up in the money supply in recent years without a corresponding rise in output will also contribute to a revival of inflation. In response to this growing concern about inflation, interest rates for long-term bonds have risen about one percentage point in just a month's time, gold has increased from $404 to over $450 per troy ounce in the same period, while silver is at its highest level since June 1984.

However, these concerns probably exaggerate the true inflation picture. Consumer prices should rise around four percent this year. Granted this is about double last year's average price increase. However, this year's expected rate is very much in line with the annual price rises of the four preceding years, 1982 through 1985, and the slowdown in inflation of the past few years can be traced to two components: energy and food prices. How these two normally volatile items—influenced by such erratic factors as the weather and OPEC—affect the overall CPI can be easily illustrated.

From 1983 to 1986, the total CPI changes varied from a low of 1.9 percent to a high of 4.3 percent. Excluding food and energy, consumer prices registered increases in the slightly higher, but narrower range of 3.9 percent to 4.9 percent. Although energy and food prices have begun to post increases, sluggish world economic growth and an oversupply of both oil and agricultural products should keep prices from climbing much further this year.

CONSUMER PRICE INFLATION (LINE) VS.
UNIT LABOR COSTS – NONFARM BUSINESS (DOT)
(PERCENT CHANGE FROM A YEAR AGO)




## . . . With A Weaker Dollar, Higher Wages . . .

What should exert some upward pressure on inflation is the continued fall of the dollar on the foreign exchange markets. By itself, the weaker dollar is a small factor, since imports account for only about 14 percent of GNP, and many foreign producers have apparently sacrificed some of their profit margins by not raising prices as much as the comparable rise in their currencies. The problem is that these increases in imported goods' prices have opened the way for domestic producers also to boost their prices rather than to enlarge their market share. For example, while the yen's rapid appreciation has forced Japanese car producers to raise prices by about 20 percent since last year, Detroit automakers also increased prices by nearly ten percent, on average, and even more for certain models.

Added push may come from rising U.S. wages and unit labor costs. Unit labor costs and inflation move in tandem (see chart) and

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understandably so, since the cost of labor input is the chief determinant of most products' prices. While wage growth has slowed during the 1980s compared with the late 1970s, this can be traced mainly to the manufacturing sector. Services-producing industries posted higher wage gains than did manufacturing in the first half of this decade. And since our economy has become increasingly service-dominated, these large gains exerted more and more inflationary pressure because they were not offset by greater productivity.

In 1986, wages in the manufacturing and services sectors rose by similar rates of 3.3 percent and 3.2 percent, respectively. However, in factories this pay raise was accompanied by a 2.7 percent gain in productivity, so their unit labor costs rose only 0.6 percent. Service industries, on the other hand, seem to have registered no gains in productivity, and the entire 3.2 percent was added to unit labor costs. Although it should be noted that productivity in the service sector is harder to measure than in manufacturing, this wage-push factor is a major reason why service prices rose 5.0 percent in 1986 vs. 1.3 percent for goods excluding energy.

## Short Term Paper Outstanding

(Millions of Dollars)

| Time Deposits of $100,000 or more Weekly Reporting Banks | Latest Week | Change Since Week Ago | Change Since Year Ago |
|---|---|---|---|
| Nationwide (4/8/87) | 158,548 | + 992 | – 2,221 |
| New York City (4/15/87) | 36,172 | – 2 | + 1,338 |
| **Commercial Paper** | | | |
| (4/15/87) | 335,388 | – 203 | + 36,038 |

## Bank Loans

(Millions of Dollars)

**Commercial and Industrial Loans**

| Weekly Reporting Large Commercial Banks | Latest Week | Change Since Week Ago | Change Since Year Ago |
|---|---|---|---|
| Nationwide (4/8/87) | 278,665 | – 1,095 | +17,606 |
| New York City (4/15/87) | 62,558 | – 17 | + 3,517 |

**Total Loans and Leases Gross Adjusted**

| | Latest Week | Change Since Week Ago | Change Since Year Ago |
|---|---|---|---|
| Nationwide (4/8/87) | 785,836 | – 4,646 | +55,778 |
| New York City (4/15/87) | 176,877 | + 3,169 | +16,476 |

## Financial Markets

| | Friday 4/24/87 | Change Since Week Ago | Change Since Year Ago |
|---|---|---|---|
| **U.S. Governments, Closing Yields:** | | | |
| 90-Day Bills† | 5.89% | + .17 | – .40 |
| 180-Day Bills† | 6.24 | + .14 | – .22 |
| Longest Bills† | 6.76 | + .37 | + .15 |
| **Recent Issues:** | | | |
| 7 1/8S 4/31/89 (When Issued) | 7.43 | NA | |
| 6 3/4S 3/31/91 | 7.90 | + .48 | |
| 7 1/2S 11/15/96 | 8.43 | + .41 | |
| 7 1/2S 11/15/16 | 8.67 | + .44 | |
| **Municipals:** | | | |
| Bond Buyer–20 Bond Index* (4/23/87) | 7.82% | – .08 | + .60 |
| Blue List Total ($ Million) | $1,831 | – $472 | –$ 137 |
| 30-Day Visible Supply ($ Million) | $3,379 | + $ 18 | –$2,311 |
| Total | $5,210 | – $454 | –$2,448 |
| **Corporates:** | | | |
| Moody's Aa Composite (4/23/87) | 9.27% | + .09 | – .06 |
| 30-Day Visible Supply ($ Million) | $6,009 | – $679 | +$3,311 |
| **Stocks:** | | | |
| **Dow-Jones Averages:** | | | |
| Industrials | 2,235.37 | – 40.62 | +399.80 |
| Transportation | 913.47 | – 10.62 | +102.50 |
| Utilities | 199.33 | – 4.78 | + 12.63 |
| 65 Stocks | 835.17 | – 14.35 | +121.33 |
| N.Y.S.E. Composite Index | 159.37 | – 3.22 | + 19.86 |
| N.Y.S.E. Avg. Daily Vol. for Week (000's) | 173,993 | – 34,830 | +26,619 |

*46% Taxable equivalent 14.48%. † Bond equivalent.

## International Rates

| EURODOLLAR DEPOSIT RATES (bid) | Friday 4/24/87 | Week Ago |
|---|---|---|
| Overnight | 6.13% | 6.19% |
| 1 month | 6.63 | 6.56 |
| 3 month | 6.94 | 6.69 |
| 6 month | 7.19 | 6.81 |
| 1 year | 7.69 | 7.13 |
| **EURODOLLAR BONDS Average Yield** | | |
| Medium Term (5 yrs.) | 8.36% | 8.31% |
| Long Term (10 yrs.) | 9.03 | 8.93 |

**FOREIGN EXCHANGE SPOT RATES**

| New York Opening (4/24/87) | Currency Per U.S. $ | Week Ago |
|---|---|---|
| Canada | 1.3310 | 1.3195 |
| France | 5.9790 | 6.0260 |
| Germany | 1.7935 | 1.8105 |
| Italy | 1280.50 | 1291.00 |
| Japan | 139.75 | 142.85 |
| Mexico | 1179.00 | 1168.00 |
| Switzerland | 1.4635 | 1.4925 |
| U.K.* | 1.6510 | 1.6305 |

*U.S. $ per U.K. pound

| MH TRADE-WEIGHTED DOLLAR (4/24/87) (Adjusted for Inflation) | Change Since Week Ago | Change Since 2/27/85 |
|---|---|---|
| | –0.3% | –5.9% |

### . . . And An Uncertain Fed Reaction

How the Federal Reserve will react if the rate of consumer price inflation remains above six percent is less certain. On the one hand, the Fed may tolerate higher inflation as the price to be paid for better economic growth both here and abroad. On the other, the central bank, being the bastion of inflation-fighting and looking to support the dollar, may choose to move in the direction of higher interest rates in order to hold the lid on prices, but at the cost of slowing down this year's already mediocre economic growth.

And for everyone else carrying a wallet, the relation between the reported increase in the consumer price index and people's perception of the pace of price changes is sometimes spurious. With last Friday's release of the March CPI, prices at the consumer level now stands 5.3 percent above their March 1985 levels. But as has been pointed out before (Financial Digest–November 10, 1986), what consumers actually consider to be inflation are the rises in prices of items they buy frequently. As such, these price changes, now measured monthly by the Manufacturers Hanover Nuisance Price Index, are over 12 percent higher than they were in March 1985. ■

## Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

| | Week Ending 4/22/87 | $ Change Since Week Ago | $ Change Since Year Ago |
|---|---|---|---|
| Reserve Bank Credit | | | |
| U.S. Gov'ts and Agencies Owned Outright & RPs | 212.588 | + 2.982 | +25.425 |
| Loans to Depository Inst. | 1.219 | + .526 | + .227 |
| Float | 1.492 | + 1.288 | + 1.176 |
| Total Reserve Bank Credit | 232.022 | + 4.822 | +27.735 |
| Treasury Deposits with Federal Reserve Banks | 4.758 | + .943 | + 2.537 |
| Currency in Circulation | 210.299 | + .169 | +15.935 |
| Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week) | 175.355 | – 3.111 | +35.542 |
| | **4/22/87** | | |
| Member Bank Reserves: | | | |
| Total Reserves Held | 58.913 | + 2.666 | +10.375 |
| Excess (Deficiency) | .928 | + .229 | + .052 |
| Net Free Reserves | .239 | – .067 | – .447 |

| Monetary Aggregates † | | % Change Since 3 Months Ago* | % Change Since Year Ago |
|---|---|---|---|
| M1 (4/13/87) | 742.1 | + 0.6‡ | + 15.4‡ |
| M2 (March '87) | 2,825.6 | + 3.7 | + 8.7 |
| M3 (March '87) | 3,525.3 | + 4.2 | + 8.0 |
| Domestic Nonfinancial Debt (4th Q'86) | 7,680.6 | + 13.8 | + 12.1 |

†Seasonally adjusted.

*Seasonally adjusted annual rate.
‡Four-week moving average.

## New York Money Market

| Offering Rates 4/24/87 | 3 Months | 6 Months | 1 Year |
|---|---|---|---|
| ‡U.S. Treasury Bills | 5.70% | 6.02% | 6.39% |
| * Federal Agencies | 6.05 | 6.22 | 6.50 |
| * Municipal Notes—High Grade (46% Taxable Equivalent) | 9.72 | 9.72 | 9.26 |
| Negotiable Time CDs Manufacturers Hanover | Rates By Arrangement | | |
| * Secondary Market—Prime | 6.50 | 7.00 | 7.30 |

| ‡Finance Company Paper—Prime | |
|---|---|
| 5- 14 days | 6.25% |
| 15- 29 days | 6.35 |
| 30- 59 days | 6.40 |
| 60- 89 days | 6.43 |
| 90-179 days | 6.41 |
| 180-239 days | 6.30 |
| 240-270 days | 6.30 |

| ‡* Bankers' Acceptances | |
|---|---|
| May | 6.50% |
| Jun. | 6.60 |
| Jul. | 6.80 |
| Aug. | 6.85 |
| Sep. | 6.85 |
| Oct. | 6.85 |

‡Industrial Paper—Prime

| | |
|---|---|
| 30- 89 days | 6.43% |
| 90-120 days | 6.50 |

†Federal Funds Effective Rate 6.30%

‡Discount basis. *Subject to availability. † Estimated.

## Selected Business Indicators

(All Dollar Figures in Billions)

| | Latest Period or End of Period | | Previous Period | Year Ago Period |
|---|---|---|---|---|
| Gross National Product (Current Dollars)* | 1st Q'87n | $ 4,339 | $ 4,259 | $ 4,149 |
| Gross National Product (1982 Dollars)* | 1st Q'87n | $ 3,735 | $ 3,696 | $ 3,656 |
| Percent Change, Annual Rate | 1st Q'87n | 4.3 | 1.1 | 3.8 |
| Change in Consumer Prices* | Mar '87n | 4.8% (1) | 8.4% (1) | – 4.8% |
| Change in Producer Prices* | Mar '87 | 4.8% | 1.2% | – 10.8% |
| Civilian Employment (Thousands of Persons)† | Mar '87 | 111,368 | 111,382 | 108,807 |
| Unemployment as % of Civilian Labor Force† | Mar '87 | 6.6% | 6.7% | 7.2% |
| Personal Income* | Mar '87n | $ 3,604 | $ 3,599r | $ 3,445 |
| Leading Indicators Composite Index (1967=100)† | Feb '87 | 187.1 | 185.8 | 175.0 |
| Industrial Production Index (1977=100) † | Mar '87n | 126.7 | 127.1r | 123.6 |
| Net Change in Consumer Installment Credit † | Feb '87 | $ 1.77 | $ 0.79 | $ 5.08 |
| U.S. Merchandise Trade Balance | Feb '87n | –$ 15.07 | –$ 12.27r | –$ 11.37 |
| Plant and Equipment Expenditures* | 2nd Q'87n | $396.22(a) | $384.02(a)r | $375.92 |
| Private Housing Starts (Thousands of Units)* | Mar '87n | 1,774 | 1,833r | 1,887 |
| New Construction Expenditures* | Feb '87 | $ 378.4 | $ 374.8 | $ 373.9 |
| Total Business Inventories † | Feb '87n | $ 660.2 | $ 659.0r | $ 651.9r |
| Total Business Sales † | Feb '87n | $ 443.8 | $ 425.1r | $ 419.6r |

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.
(1) Indicates new series.

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Commitment

Great Cause, Great Golf!

The Manufacturers Hanover
Westchester Classic
Westchester Country Club
Harrison, N.Y.
June 8-14, 1987

During the last 20 years, the Manufacturers Hanover Westchester Classic has raised over $10 million for the local hospitals. This is a tribute to all the volunteers, fans and corporations who continually support this great charitable event.

This year, defending champion Bob Tway and other top pros from the PGA Tour will compete for $600,000 in prize money.

Tickets are on sale at all the participating hospitals through June 5, thereafter at the gate. Use your Mastercard or Visa Card, by calling (212) 808-8519, Monday through Friday, 9 a.m. -5 p.m.

Spectators are urged to arrive early and be among the first 1500 each day to receive a free visor at the gate. **Make it a point to stop by the Expo '87 tent behind the 18th green.**

Benefiting Hospitals: United, Lawrence Auxiliary, New Rochelle, Northern Westchester, Phelps Memorial, St. Agnes, St. John's, St. Joseph's, St. Vincent's, Blythedale Children's, Greenwich, Mount Vernon, White Plains, Yonkers General, Peekskill and Putnam Hospital Center.

BUICK

NABISCO GRAND PRIX

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